COMMITTEE ON LEGISLATIVE RESEARCH
OVERSIGHT DIVISION

FISCAL NOTE

L.R. No.: 0122-03
Bill No.: HCS for HJR 8
Subject: Taxation and Revenue - General; Constitutional Amendments
Type: Original
Date: March 9, 2011

Bill Summary: Proposes a constitutional amendment relating to revenue neutral replacement of all taxes on income with an amended sales and use tax.

FISCAL SUMMARY

ESTIMATED NET EFFECT ON GENERAL REVENUE FUND			
FUND AFFECTED	FY 2012	FY 2013	FY 2014
General Revenue	$0 or (More than $7,000,000)	$0 or ($211,499)	$0 or ($855,902)
Total Estimated Net Effect on General Revenue Fund	**$0 or (more than $7,000,000)**	**$0 or ($211,499)**	**$0 or ($855,902)**

ESTIMATED NET EFFECT ON OTHER STATE FUNDS			
FUND AFFECTED	FY 2012	FY 2013	FY 2014
Total Estimated Net Effect on Other State Funds	**$0**	**$0**	**$0**

Numbers within parentheses: ( ) indicate costs or losses.
This fiscal note contains 24 pages.

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2012	FY 2013	FY 2014
Total Estimated Net Effect on All Federal Funds	**$0**	**$0**	**$0**

ESTIMATED NET EFFECT ON FULL TIME EQUIVALENT (FTE)			
FUND AFFECTED	FY 2012	FY 2013	FY 2014
General Revenue	0	1	8
Total Estimated Net Effect on FTE	**0**	**1**	**8**

☒ Estimated Total Net Effect on All funds expected to exceed $100,000 savings or (cost).

☒ Estimated Net Effect on General Revenue Fund expected to exceed $100,000 (cost).

ESTIMATED NET EFFECT ON LOCAL FUNDS			
FUND AFFECTED	FY 2012	FY 2013	FY 2014
Local Government	**$0**	**$0**	**$0**

FISCAL ANALYSIS

ASSUMPTION

Officials from the **Office of Administration - Budget and Planning (BAP)** stated this proposal should not result in additional costs or savings to the Division of Budget and Planning.

This proposal, upon voter approval, eliminates the taxes listed below beginning January 1, 2015.
- Corporate income taxes are repealed immediately.
- Individual income taxes are decreased 25% per year, to be eliminated in full January 1, 2019.
- Corporate franchise taxes.
- All existing state sales and use taxes. However, the sales tax on used motor vehicles is to be phased out at 33-1/3% per year until eliminated by January 1, 2019.
- Repeals all tax credits except the circuit breaker.

Lost state revenues are to be replaced by a new state sales tax of 4% to no more than 7%, holding revenues substantially neutral when compared to the average collections of the repealed taxes in the previous five fiscal years. This sales tax shall apply to any goods or services, including rents, but:
- Excludes those used as business inputs, or for an investment purpose.
- Excludes intangible personal and used property.
- Excludes component parts & ingredients.
- Excludes tuition and fees for K12 and higher education.
- Excludes motor fuel purchases subject to excise tax.
- Excludes insurance premiums
- Includes all component parts of residential housing.

BAP notes that this proposal intends the new sales tax to generate revenues substantially equal to those collected in FYs 10-14. Assuming neutrality is achieved, current projections call for revenues in FY 12 to be roughly 9% below the levels collected in FY 08, an extraordinary decline which would not have happened except for the recession which began in 2007. This proposal may not allow for state revenues to recover from the unprecedented declines of FYs 09-10, especially if the General Assembly does not adopt sales tax rate adjustments as recommended by the State Treasurer in a timely fashion. While there is a mechanism for a rate adjustment at specified intervals, there is no mechanism proposed for making up any revenue shortfalls.

This proposal may make it difficult for the state to provide the level of services currently demanded and those demanded in the future. A shortfall of this nature would jeopardize the

ASSUMPTION (continued)

state's ability to make timely payments on its obligations, including those to public schools, hospitals, and public safety providers. Untimely payments could jeopardize the state's AAA bond rating; a lowered bond rating will cause state costs to increase.

This proposal attempts to hold dedicated sales tax revenues and local sales tax revenues harmless. The State Treasurer's office is to recalculate rates, and make recommendations to the General Assembly, to achieve this end. However, if the appropriate bills do not pass the General Assembly in a timely fashion, local and dedicated revenues may experience substantial shortfalls.

While the sales tax rate on new vehicles would increase, the rate would be zero on used vehicles. This would create a strong incentive for consumers to eschew purchases of new vehicles, which would adversely impact funding for road construction and maintenance.

Because of the reduced points of tax collection and the complicated sales tax rebate system, numerous new opportunities for tax fraud may be invented. The DOR can provide a fuller discussion of such issues, the costs that might be incurred to prevent such fraud, and the considerable administrative costs that will be necessary to transition to the new tax system. Conversely, it is likely that taxpayers that are currently evading income taxes will face higher tax payments as a result of this proposal.

The DED and other agencies that administer tax credits can better address the impact of the loss of these programs.

Calculating a Sales Tax Rate

The proposal calls for a 7% sales tax rate on a newly defined sales tax base. However, data that is sufficiently detailed to estimate consumer spending while excluding difficult-to-define concepts such as business inputs, rents, and investment is extremely difficult to access. Recent literature available on this topic suggests this rate is likely too low. A technical essay available on the Show-Me Institute website suggests a rate of 10-12% would be a revenue-neutral rate. Estimates from other groups, such as the Institute for Taxation and Economic Policy also suggest something greater than 11%.

Estimating the Consumption Base

BAP estimates the consumption base using a methodology suggested by ITEP, starting with national personal consumption as reported in the US BEA's NIPA tables as reported by the BEA in December 2010, excluding items that are non-taxable under federal law or under the proposal

ASSUMPTION (continued)

(such as higher education spending). BAP estimates the loss due to explicit avoidance activities, such as internet purchases, traveling across state lines, or the purchase of used goods, as 10%; this figure is entirely arbitrary. MO expenditures are assumed to be 1.77% of national expenditures, based on MO's portion of personal income in 2009 as reported by the BEA in December 2010. BAP estimates the consumption base to be $105.138B as in Table 1. At the 4% rate described in the proposal, this would generate just over $4.2B in revenues. At the 7% rate codified in the proposal, this would generate just under $7.36B in revenues.

The calculations presented assume current consumption patterns will remain the same. This is highly unlikely. Changes in income and final prices will impact consumer choices, but the possible effects are unclear, and potentially harmful to the consumption base:

- The proposal increases prices, via a new sales tax, for many products and services. These include but are not limited to food for home consumption, medical care and pharmaceuticals, domestic utilities and telecommunications, rents, daycare providers, consumer legal and financial services, realty services, repair services, and personal care services.
- According to US Census Bureau data, roughly two-thirds of MO's population lives in a county bordering another state. The potential for retail sales leakage is high since it may be easy for consumers in these counties to seek lower tax rates in other states. The incentive to do so would increase as the price of the product increases.
- The growing use of electronic commerce will dampen the growth of easily taxable consumption.
- There is a great amount of uncertainty as to the incidence of this tax. In other words, it is not clear which taxpayers will actually pay it. Taken at face value, it appears taxpayers who consume the most will pay the most. However, those with the greatest ability to consume also have the greatest ability to avoid the tax by making their purchases outside state boundaries. In this case, the burden is shifted to the lower- and middle-class families. However, this proposal specifically instructs legislators to provide relief to households to benefit low-income taxpayers, leaving the burden of the tax to fall on middle-class families.
- This proposal may adversely impact the federal tax liability of state-wide taxpayers. Currently, state income taxes paid are deductible from federal taxable income. According to the IRS Statistics of Income, an estimated $4.46 billion in state and local income taxes were deducted in tax year 2008. (A much smaller amount of sales taxes was also deducted.) This increase in federal taxes might have a detrimental impact on the consumption base.

ASSUMPTION (continued)

Revenues to be Replaced

BAP estimates the revenues to be replaced as in Table 2. Note that Table 2 includes several revenue sources in addition to General Revenues, in an effort to provide an estimate of the total statewide sales tax rate. Revenues include:

- Bank and Insurance taxes. These taxes may be considered income taxes as repealed in section 2, even though specifically listed in section 5.
- Gaming gross receipts taxes. These taxes may be considered income taxes as repealed in section 2, even though specifically listed in section 5.
- Motor Vehicle Sales taxes. (Currently, sales taxes on vehicles are dedicated to roads, but as discussed above, the impact of this proposal on road funding is unclear.)

The table shows that revenues to be replaced approach those generated by the proposed 7% sales tax shown in Table 1. Should the General Assembly fail to adjust the rate upward from the 4% starting point, substantial revenue shortfalls would occur.

Table 1.

Estimating the Base	**NIPA Table**	**Amount ($B)**
National PCE	2.45	10,001.3
Higher Education (specifically exempted)	2.4.5: 101	(145.5)
K-12 Education	2.4.5: 102	(39.7)
Motor Fuel	2.4.5; 36	(280.8)
Insurance Premiums	2.4.5: 90	(308.6)
Health Care Spending by the Govt (not taxable under federal law)	3.16: 028	(1,029.1)
Free checking other financial services	2.4.5: 088	(271.2)
Rental Value of owner-occupied housing	2.4.5: 052	(1,211.9)
Food Stamps (not taxable under federal law)	3.12: 021	(54.6)
Spending by charities on behalf of individuals	2.5.5: 132	(258.9)
Interstate air & ground transportation (not taxable under federal law)	2.5.5: 064	(45.1)
Foreign travel by US citizens	2.4.5: 109	(105.4)
Foreign travel into US	2.4.5: 110	124.5
Value of new home sales	5.2.5: 019	352.1
Net taxable base		**6,727.1**
Assume 10% loss for avoidance, purchases of used goods		5,940.0
MO share 1.77%:		**105.138**
Revenues At 4% Rate		**4,205,520,000**
Revenues At 7% Rate		**7,359,660,000**

ASSUMPTION (continued)

Table 2.

Sources	FY 2010
Individual Taxes	5,495,341,696
Individual Refunds	(1,050,238,448)
Corporate Taxes	502,091,318
Corporate Refunds	(214,417,694)
Insurance Taxes	233,637,079
Bank Taxes	11,016,515
GR Sales and Use Taxes (DOR CAFR)	1,790,181,504
Sales Tax Refunds	(59,962,469)
Motor Vehicles Sales Taxes	193,298,505
Gaming Taxes	334,287,278
Revenues to Be Replaced	**7,235,235,283**

Calculation of the Prebate

This proposal states the General Assembly may provide a prebate of up to $2800 per qualified household member (which is undefined in this proposal), up to a maximum of $11,200 per household (also undefined in this proposal). Estimating MO's population at 5.9 million, a $2,800 prebate for each person would cost $16.25B. Estimating MO's households at 2.3 million, an $11,200 prebate would cost $25.76 billion. Clearly, these figures are unaffordable based on the estimated sales tax collections. The General Assembly could not implement a prebate at these levels.

Given that no further direction is provided, BAP cannot calculate the potential cost of the prebate or the associated budgetary impacts.

Officials from the **Department of Transportation (MoDOT)** anticipates a negative impact from removing the sales and use tax on used vehicles and limiting new motor vehicle sales and use tax to the average of the five preceding fiscal years. This would be an impact of $33 M to MoDOT in FY 2015; $115 M in FY 2016 and $168 M in FY 2017. Plus there would be an impact to the cities and counties; $5 M in FY 2015; $17 M FY 2016 and $24 M FY 2017.

ASSUMPTION (continued)

The department also has concerns that the Missouri Highways and Transportation Commission would likely face downgrade of its rating as it relates to its $3.3 billion of outstanding State Road bonds due to such a significant change in revenue for the department.

Oversight assumes the new sales and use tax would be established in such a way that revenue neutrality would occur for Total State funds as well as revenue within each fund.

Officials from the **Department of Revenue (DOR)** have the following comments and assumptions:

Section 4(d)

Beginning January 1, 2015, no tax will be imposed on income, except as established in the legislation.

In lieu of the repealed taxes, a tax will be imposed on the consumption and use of taxable property and services.

No tax credits shall be authorized after January 1, 2015.

No authorized tax credit other than for senior citizens property tax relief shall be allowed after the elimination of the individual income tax.

This legislation defines the terms:

- Taxable property and services,
- Purchased for business purpose in a trade or business,
- Purchased for an investment purpose

No tax shall be imposed under this section for:

- Motor fuel purchases subject to an excise tax;
- Premiums or fees paid on valid insurance policies but only if the insurance company does not claim business-to-business exemptions on purchases; or
- Property for which the tax authorized under this section has been collected due to a prior taxable transaction.

The general assembly shall provide by law for determining the scope of taxable services and for otherwise implementing the provisions of this section prior to January 1, 2015.

An adjustment will be calculated to ensure that the amount of revenue received is substantially equal to the amount of revenue that would have been generated by the taxes repealed under this section averaged over the five immediately preceding state fiscal years.

The Department will recalculate local political subdivision tax rates affected by this section no later than August 31, 2014, unless the local political subdivision has submitted

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a proposal to increase any such local tax rates and has received majority approval from the voters for the increase.

The Department shall submit the recalculated rates to the state treasurer for approval.
The state treasurer shall publish the approved sales tax rates for the local political subdivisions no later than November 30, 2014.
The local government can request a recalculation one time within a twenty-four month period.
The department of revenue and the state treasurer shall repeat the recalculation process of the local sales tax rates by August 31, 2015, and November 30, 2015, respectively.
The Proposition C tax rates undergo a one-time calculation by the state treasurer.
For the tax year beginning January 1, 2015, the general revenue sales tax rate shall be four percent.
Taxes being replaced include:

- Corporate income taxes,
- Withholding and individual income taxes of at least 25% per year and eliminated completely no later than January 1, 2019,
- Corporation franchise and bank franchise taxes,
- All existing state sales and use taxes with a one-third reduction on used motor vehicles with full elimination no later than January 1, 2019.

The general assembly may provide a method for calculating and providing sales tax rebates or "prebates" to allow a portion of taxable purchases made by Missouri residents to be exempt from the tax authorized under this section. The maximum rebate is $2,800 per qualified household member and $11,000 per qualified household.
The department of revenue will implement the provisions of these sections.
The revisor of statutes, in conjunction with the department of revenue, the state tax commission, and other tax-related agencies and departments, shall prepare and submit to the committee on legislative research a proposed bill repealing those provisions of law which are deemed unenforceable or unnecessary under the provisions of this section.
Provisions of this section are severable if found to be unconstitutional.
The Department will need to make programming changes to various tax processing systems.

NOTE: The following impacts will not be realized until FY15 because the legislation has an effective date of January 1, 2015. The department must hire staff and train new employees prior to January 1, 2015.

ASSUMPTION (continued)

Personal Tax:

For FY 12 – Personal Tax will retain 100% of existing staff to continue the processing and collection duties of individual income tax
For FY 13 – Personal Tax will retain 100% of existing staff to continue the processing and collection duties of individual income tax
For FY 14 - Personal Tax will retain 100% of existing staff to continue the processing and collection duties of individual income tax.
For FY 15 – Personal Tax will retain 100% of existing staff to continue the processing and collection duties of individual income tax
For FY 16 – Personal Tax will retain 100% of existing staff to continue the processing and collection duties of individual income tax
For FY 17 – Personal Tax will retain 100% of existing staff to continue the processing and collection duties of individual income tax
For FY 18 – Personal Tax will retain 100% of existing staff to continue the processing and collection duties of individual income tax
For FY 19 – Personal Tax will retain 100% of existing staff to continue the processing and collection duties of individual income tax

Collections & Tax Assistance (CATA):
Section 4(d)5(4)

CATA anticipates increased contacts regarding the rate changes / adjusted returns.

- One (1) Tax Collection Technician I (Range 10, Step L) for every additional 15,000 contacts annually on the delinquent tax line
- One (1) Tax Collection Technician I (Range 10, Step L) for every additional 15,000 contacts annually on the non-delinquent tax line
- One (1) Revenue Processing Technician I (Range 10, Step L) for every additional 4,800 contacts annually in the Tax Assist Offices
- One (1) Revenue Processing Technician I (Range 10, Step L) for every additional 8,300 registrations/maintenance to business tax accounts
- One (1) Revenue Processing Technician I (Range 10, Step L) for every additional 24,000 contacts annually to the registration phone line

Section 4(d)6

Based on the assumption the taxpayer must claim the tax rebate/prebate, CATA will require:

- One (1) Tax Collection Technician I (Range 10, Step L) for every additional 15,000 contacts annually on the non-delinquent tax line

ASSUMPTION (continued)

- One (1) Revenue Processing Technician I (Range 10, Step L) for every additional 4,800 contacts annually in the Tax Assist Offices

The registration area would be impacted because including all services as a taxable product would greatly expand the types of businesses that will need to register for sales and use tax.

Assuming the number of businesses required to register for sales tax doubles, CATA could see the following impact:

- FY12 - No impact
- FY13 - No impact
- FY14 - No impact
- FY15 - Based on the assumption of doubling the number of businesses, for registration, contacts, and collection effort CATA will need an additional 88 temporary employees (CATA's FY09 sales use tax and registration FTE impact was 44) Training will begin in October of 2014.

Corporate and Withholding Tax:

For FY 12 - 100% of existing staff will need to be retained in the Withholding Tax Section and the Corporate Tax Section to continue the processing and collection duties of withholding, financial institutions tax and corporate tax.

For FY 13 - 100% of existing staff will need to be retained in the Withholding Tax Section and the Corporate Tax Section to continue the processing and collection duties of withholding, financial institutions tax and corporate tax.

For FY 14 - 100% of existing staff will need to be retained in the Withholding Tax Section and the Corporate Tax Section to continue the processing and collection duties of withholding, financial institutions tax and corporate tax.

For FY 15 - 100% of existing staff will need to be retained in the Withholding Tax Section and a portion of existing staff will need to be retained in the Corporate Tax Section to continue the processing and collection duties of withholding, financial institutions tax and corporate tax.

For FY 16 - 100% of existing staff will need to be retained in the Withholding Tax Section and a portion of existing staff will need to be retained in the Corporate Tax Section to continue the processing and collection duties of withholding, financial institutions tax and corporate tax.

For FY 17 - 100% of existing staff will need to be retained in the Withholding Tax Section and a portion of existing staff will need to be retained in the Corporate Tax Section to continue the processing and collection duties of withholding, financial institutions tax and corporate tax.

ASSUMPTION (continued)

For FY 18 - 100% of existing staff will need to be retained in the Withholding Tax Section and a portion of existing staff will need to be retained in the Corporate Tax Section to continue the processing and collection duties of withholding, financial institutions tax and corporate tax.
For FY 19 - 100% of existing staff will need to be retained in the Withholding Tax Section and a portion of existing staff will need to be retained in the Corporate Tax Section to continue the processing and collection duties of withholding, financial institutions tax and corporate tax.

Sales, Excise and Business Tax:

The Department must recalculate local sales tax rates and publish those rates by August 31, 2014. It will need to hire an economist in FY13 to begin working on the adjusted rates.
The following impact is based upon the assumption that the workload for sales and use tax will double because of the additional filers. Based upon FY09 program costs, which include processing, correspondence, error correction, refunds, etc., Business tax will need an additional 97 temporary employees for sales and use tax.
The Department assumes that although the new sales tax would go into effect January 1, 2015, only a small amount of the staff responsible for corporate tax would be available for reallocation in FY16, and even then, it may be only a fraction of the employees. Therefore, temporary staff will be needed until the current staff can be reallocated:

- FY12 – No impact
- FY13 – No impact
- FY14 – No impact
- FY15 – Business tax will need 97 temporary employees. Training will begin in October of 2014. These would be temporary employees however because they will be employed for nine months, benefits will be provided.
- FY16 – For the first half of the year Business tax will need the 97 temporary employees and for the second half Business tax will need 92 temporary employees. The reduction for the second half of FY15 is based upon the assumption that 5 permanent staff will now be available for reallocation.
- FY17 and beyond-The Department will move staff as they become available from the expired tax types.

If the number of new filers should more than double, then the amount of additional resources will increase proportionately

ASSUMPTION (continued)

Field Compliance:

- In fiscal year 2010, Field Compliance conducted 2,350 sales and use tax audits. To conduct double that amount, (4,700 sales and use tax audits), it would be necessary to double audit enforcement staff, including additional instate and out of state personnel. Currently, Field Compliance has 160 assigned positions with an approximate payroll of $7.4 million. The addition of 160 new positions would increase Field Compliance to 320 positions and a payroll of approximately $14.0 million.

- Each additional employee would have start up costs which would include a new computer, file cabinet, desk, chair, side chair, calculator, and on-going supplies. The approximate cost for 160 new employees would be $454,080. The travel and operating budget could potentially double by moving the budget from $400,000 to potentially $800,000. This would bring the approximate Expense and Equipment cost to approximately $1.2 million.

- The Department would need to expand and possibly move each in-state and out of state audit office facility to accommodate the increase in personnel. The estimated cost would double fiscal year 2010's amount of $450,000 to $900,000.

Legal Services

- For FY 12 – No impact
  For FY 13 – No impact
  For FY 14 – No impact
  For FY15 – Based on the presumption of doubling the number of businesses licensed to collect and remit sales tax, there will be a substantial increase in the caseload. The income tax cases will decrease over time, but they will continue for the next few years. Legal services will need to add four additional attorneys and two support staff.

Prebate

Because the prebate will be provided by subsequent legislation, the Department cannot determine what resources will be required with any certainty. But additional resources above those already identified will be required.

DOR assumes the cost of this proposal is not within the period of the fiscal note. Space for approximately 350 personnel will be required in fiscal year 2015.

<u>ASSUMPTION</u> (continued)

Officials at the **Office of the Secretary of State** (**SOS**) assume unless a special election is called for the purpose, Joint Resolutions are submitted to a vote of the people at the next general election. If a special election is called to submit a Joint Resolution to a vote of the people, section 115.063.2 RSMo requires the state to pay the costs. Article III section 52(b) of the Missouri Constitution authorizes the general assembly to order a special election for measures referred to the people and Article XII section 2(b) authorizes the governor to call a special election to submit constitutional amendments to a vote of the people.

The SOS is required to pay for publishing in local newspapers the full text of each statewide ballot measure as directed by Article I, Section 26, 27, 28 of the Missouri Constitution and Section 116.230-116.290, RSMo. The Secretary of State's office is provided with core funding to handle a certain amount of normal activity resulting from each year's legislative session. Funding for this item is adjusted each year depending upon the election cycle with $1.3 million historically appropriated in odd numbered fiscal years and $100,000 appropriated in even numbered fiscal years to meet these requirements. The appropriation has historically been an estimated appropriation because the final cost is dependent upon the number of ballot measures approved by the General Assembly and the initiative petitions certified for the ballot. In FY 2011, at the August and November elections, there were 6 statewide Constitutional Amendments or ballot propositions that cost $1.02 million to publish (an average of $170,000 per issue). Therefore, the Secretary of State's office assumes, for the purposes of this fiscal note, that it should have the full appropriation authority it needs to meet the publishing requirements. However, because these requirements are mandatory, we reserve the right to request funding to meet the cost of our publishing requirements if the Governor and the General Assembly change the amount or eliminate the estimated nature of our appropriation.

Oversight has reflected in this fiscal note, the state potentially reimbursing local political subdivisions the cost of having this joint resolution voted on during a special election in fiscal year 2011. This reflects the decision made by the Joint Committee on Legislative Research, that the cost of the elections should be shown in the fiscal note. The next scheduled general election is in February (FY 2012). It is assumed the subject within this proposal could be on that ballot; however, it could also be on a special election called for by the Governor. Therefore, Oversight will reflect a potential election cost reimbursement to local political subdivisions in FY 2012.

To estimate the expense the state would incur for reimbursing local political subdivisions for a special election, Oversight requested expense estimates from all election authorities for an election. Eighty-six out of the one hundred fifteen election authorities responded to Oversight's request. From these respondents; the total election expense that would have to be reimbursed by

ASSUMPTION (continued)

the state government is over $7 million. Therefore, Oversight will reflect a potential cost borne by the state in FY 2012 of over $7 million for reimbursement to the local political subdivisions. Oversight assumes the Governor could call for a special election to be held prior to February , 2012 regarding this joint resolution; however, if a special election is not called, the subject will be voted on at the general election in February 2012.

Officials from the **Department of Higher Education (DHE)** assume this proposal will have no direct foreseeable fiscal impact on their agency.

Officials from the **University of Missouri - Columbia** assume the financial impact to the University upon passage of the proposal should be revenue neutral assuming that the revenue generated by imposition of the sales and use tax is approximately equal to the revenues lost as a result of the prohibition on the taxation of income. However, the base tax years for equivalency are low tax years for which there were not sufficient general tax revenues to fund current general revenue appropriations resulting in negative impact on higher education. To recalibrate a differential tax system against the low tax years could have detrimental effect on higher education.

Officials from the **State Tax Commission** assume the proposal would not fiscally impact their agency.

In response to a similar proposal in 2010, HJR 56, 3038-02n, officials from **Legislative Research** assumed the proposal will not create a fiscal impact; however, additional compensatory time may be needed for staff attorneys if the proposed clean-up bill is done during regular session.

In response to a similar proposal in 2010, HJR 56, 3038-02n, officials from **Cass County** assume this will not impact current sales taxes that exist in local governments. It is assumed that this proposal just replaces the state income tax with a state-wide sales tax (as defined). Thus, if Cass County is assuming correctly, and its sources of sales tax revenue remain in place, there is no fiscal impact on the county budget.

Officials from **St. Louis County** state local government sales taxes are not subject to an unrealistic hard cap, though the averaging of recession level revenues would be a negative factor. It’s difficult to predict the city by city ramifications of these radical changes. There would be winners and losers. However, the overall negative impact to the County Government would come from the following factors:

ASSUMPTION (continued)

1. Reductions in state funding to local government due to failure to reach revenue neutrality. (Est. 10% reduction in state funds to county government).
2. Reductions in local sales tax revenue due to reduced after tax income of St. Louis County households because of major shift of state tax burden to households. (Est. 3% reduction in sales tax).
3. Reductions in local sales tax revenue due to tax avoidance and evasion (purchases in Illinois, and purchases attributed to businesses). (Est. 5% reduction)
4. Reduction in local sales and property tax revenue due to negative impact on major medical centers in metropolitan St. Louis. (Est. 2% reduction in sales tax - 1% reduction in property tax).
5. Reductions in local property tax revenue due to declining property values caused by taxation of new home sales. (Est. 2% reduction in property tax).

Also, under the proposal, it is possible that the tax on medical treatment would be deemed to be the responsibility of insurers, not patients. If that is the case, County government, like any major employer, would face a huge increase in health care costs.

Officials from the **City of Independence** assume the city is not authorized by Statute to levy a tax on income or earnings. This proposal will replace a progressive tax (income) with a regressive tax (sales). Therefore, the greater tax burden is placed on those with a lower income.

Officials from the **City of Kansas City** assume this proposal will have no fiscal impact on their city.

Officials from the cities of **Cape Girardeau**, **Kirksville**, **Poplar Bluff** as well as the counties of **Cape Girardeau**, **Franklin**, and **Jasper** did not respond to our request for fiscal impact.

Officials from the **Office of the Governor** assume the proposal would not fiscally impact their agency.

Officials from the **Office of the Attorney General** assume that the costs associated with the adoption of this proposal are unknown.

Officials from the **Department of Natural Resources (DNR)** state their Parks and Soils sales tax funds are derived from one-tenth of one percent sales and use tax pursuant to Section 47(a) of the Missouri Constitution. It appears that the intent of Section 4(d).4. is to allow for the conservation sales tax and the soil and parks sales tax to be recalculated to produce substantially

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the same amount of revenue. If that is the intent, then for purposes of this fiscal note, the department would not anticipate a direct fiscal impact from this provision.

If that is not the intent of this proposal and DNR's parks and soils sales tax is eliminated as a result of this proposal, then there would be a significant fiscal impact to the department. Funding would have to be sought to replace the monies currently collected from the department's sales and use tax pursuant to Section 47(a) of the Missouri Constitution. The department assumes the Department of Revenue would be better able to estimate the potential fiscal impact.

This proposal would also appear to eliminate all sales tax exemptions. Currently, the State of Missouri is a tax-exempt entity. If this department is required as a result of this proposal to pay the newly created 7% sales tax on the purchase of all goods and services, then there would be a significant unknown fiscal impact to the department. Each state agency's operating budget would increase substantially. The department assumes the Office of Administration would be better able to estimate the amount of fiscal impact from this provision for each department.

Officials from the **Department of Economic Development - Missouri Housing Development Commission (MHDC)** assume this proposes a constitutional amendment in 2012 that would disallow the issuance of any tax credits after 2014 and the redemption of any issued tax credits after 2018. The proposal would not itself have any fiscal impact to MHDC. If the amendment were to pass the potential impacts would be as follows:

The LIHTC and AHAP tax credits (which are used to raise private equity to fund the development of affordable rental housing for low- and moderate - income Missouri residents) may be redeemed over the course of 10 years. An equity investor who provides funding for a LIHTC development receives its tax credit over the course of 10 years, each year receiving 1/10th of its total tax credit amount. Conversely, while an AHAP tax credit may be redeemed immediately, it has a 10-year carry-forward, meaning that an AHAP investor is entitled to use this tax credit to offset the investor's tax liability for any or all of the 10 years following issuance of the credit.

MHDC anticipates that passage of HJR 8 would result in lawsuits being brought by investors seeking to ascertain their rights to redeem already-issued LIHTC and AHAP tax credits for the full 10-year redemption period the investors expected at the time they provided funding for the affordable housing developments. The state could incur litigation costs if this were to occur. If the state were to lose such a case it could result in a significant cost if the state could have to compensate the investors for their loss of benefits.

ASSUMPTION (continued)

MHDC further anticipates that the amount an investor would be willing to pay for future tax credits would be seriously depressed immediately upon passage of HJR 8, because of investors' recognition that implementation of the constitutional amendment would terminate the redemption of all tax credits in 2018 and thus that no LIHTC or AHAP tax credits issued after 2008 would be allowed to receive a full 10-year redemption period.

Officials from the **Department of Economic Development** assume this proposal repeals the existing state income tax and replaces it with a sales and use tax. The proposal prohibits the authorization of all tax credits after January 1, 2015, with the exception of the senior citizens property tax relief. Nearly all tax credit and other tax-related incentive programs administered by the Department of Economic Development's Business and Community Services Division would be impacted by this proposal, including Missouri Quality Jobs, Missouri Manufacturing Jobs Act, Enhanced Enterprise Zone, Development Tax Credit, Rebuilding Communities Neighborhood Preservation, Neighborhood Assistance Program, Wine & Grape Tax Credit, Youth Opportunities, Brownfield Remediation, and the Historic Preservation Tax Credit. This proposal would also impact several programs that provide assistance for local economic development through state revenue generated by the project, including the State Supplemental Tax Increment Financing program (TIF), the Missouri Downtown Economic Stimulus Act (MODESS), and the Downtown Revitalization Preservation Program (DRPP).

The Department assumes an unknown fiscal impact over $100,000.

Officials from the **State Treasurer's Office (STO)** assume they would rely heavily on information provided by the Department of Revenue (DOR) in their calculations, and would be required to hire additional staff and acquire technology to adequately review any sales tax rates submitted by the DOR for approval. Additionally, if a local political subdivision requested a recalculation of the sales tax rate, the STO would have to rely on the DOR to provide the necessary information to support any recalculations.

Calculations required of the STO by this proposal would not begin until fiscal 2015 making the cost to implement this proposal outside the timeframe, however, the STO assumes they would have to hire the necessary staff to perform the required calculations or contract with an entity for the same purpose during fiscal year 2014 in order to review fiscal years 2011 through 2014 prior to the implementation date. Based on our estimates, STO assumes there would be a cost of $855,900 to General Revenue in FY 2014 and similar costs for all years after plus any adjustments for increases in state employee salaries and fringe benefits.

ASSUMPTION (continued)

If the proposal were within the scope of this fiscal note **Oversight** would range the fiscal impact to the Department of Revenue from $0 (resolution is not passed by public vote) to their estimate. Oversight also assumes the proposal would be implemented in such a way that sales tax revenues to the state as well as local political subdivisions would be equivalent to the lost revenue from income tax, local earning tax, existing sales tax, franchise tax, and bank franchise tax.

Oversight assumes this proposal will not change Total State Revenues.

FISCAL IMPACT - State Government	FY 2012 (10 Mo.)	FY 2013	FY 2014
GENERAL REVENUE			
Costs - Department of Revenue			
Personnel (1 FTE - Temporary)	$0	$0 or ($57,097)	$0
Fringe Benefits (FICA)	$0	$0 or ($29,885)	$0
Expense and Equipment	$0	$0 or ($10,434)	$0
Programming Changes	$0	$0 or ($114,083)	$0
Total Costs - DOR	$0	$0 or ($211,499)	$0
Costs - State Treasurer's Office			
Personnel (8 FTE)	$0	$0	$0 or ($453,7630)
Fringe Benefits	$0	$0	$0 or ($237,500)
Expense and Equipment	$0	$0	$0 or ($164,639)
Total Costs - State Treasurer's Office	$0	$0	$0 or ($855,902)
Expense - reimbursement of local political subdivisions for special election costs	$0 or (More than $7,000,000)	$0	$0
ESTIMATED NET EFFECT TO THE GENERAL REVENUE FUND	**$0 or (More than $7,000,000)**	**$0 or ($211,499)**	**$0 or ($855,902)**
Estimated Net FTE	0	1	8

FISCAL IMPACT - Local Government	FY 2012 (10 Mo.)	FY 2013	FY 2014
LOCAL POLITICAL SUBDIVISIONS			
Income - cost reimbursement from the State for special election	$0 or More than $7,000,000	$0	$0
Expense - cost for special election	$0 or (More than $7,000,000)	$0	$0
ESTIMATED NET EFFECT TO LOCAL POLITICAL SUBDIVISIONS	**$0**	**$0**	**$0**

FISCAL IMPACT - Small Business

It is unclear what the impact will be on small business.

FISCAL DESCRIPTION

Upon voter approval, this proposed constitutional amendment phases out the state individual income tax and replaces the corporate income tax, corporation franchise and bank franchise taxes, and state sales and use tax with a fair sales tax of up to 7% on retail sales of new tangible personal property and taxable services. Beginning January 1, 2015, the state sales tax rate will be 4% and will gradually increase annually over the next four years to make the tax revenue-neutral and to provide continued funding for programs. The individual income tax will decrease 25% per year until eliminated based on the average collections over a five-year period. The sales tax on used motor vehicles will be phased out over a period of time but must be by January 1, 2019. Property purchased to be a component part or ingredient of a new tangible personal property to be sold at retail, federal government purchases, business-to-business transactions including agriculture, purchases for investment, tuition and fees for education, purchases of motor fuel when subject to an excise tax, certain insurance premiums or fees, and purchases of used tangible personal property will be exempt from the new sales tax while all other exemptions will be eliminated. No tax credits will be authorized after January 1, 2015, and no authorized tax credits, other than the senior citizens property tax credit, will be allowed after the elimination of the

DESCRIPTION (continued)

individual income tax. The conservation sales tax, the soil and parks sales tax, Proposition C sales tax, and local sales taxes will be recalculated to produce substantially the same amount of revenue. Each qualified household member will receive a sales tax rebate. The amount of the annual rebate will be $2,800 per taxpayer with a maximum rebate of $11,200 per household until 2019 when the rebate amount will be increased based on the increase in the federal Consumer Price Index in the previous year.

The resolution provides a process for the approval or rejection of the State Treasurer's recommendation for the adjusted state sales tax rate by the General Assembly and modification of existing state taxation statutes by the Revisor of Statutes.

This legislation is not federally mandated, would not duplicate any other program and would not require additional capital improvements or rental space.

SOURCES OF INFORMATION

Office of Administration - Budget and Planning
Department of Transportation
Department of Revenue
Office of the Secretary of State
Department of Higher Education
University of Missouri
Department of Economic Development
State Tax Commission
Office of the State Treasurer
Office of the Governor
Office of the Attorney General
Department of Natural Resources
City of Kansas City
St. Louis County
City of Independence

NOT RESPONDING:

Legislative Research
Cape Girardeau
Cass County
Kirksville
Poplar Bluff
Cape Girardeau County
Franklin County
Jasper County

Mickey Wilson

Mickey Wilson, CPA
Director

VL:LR:OD (12/02)

March 9, 2011